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Serving Your Personal Investment Needs Since 2003

March 10, 2008

We are experiencing a rapid and forced de-leveraging in the credit markets today, having increased in severity over the past 6 months. The end date to this de-leveraging process is not clear; nor are the consequences of this de-leveraging process well defined.

For us, as retail investors, our greatest concern comes from the deflating supply of money in the financial system. If the supply of money contracts in a cascading manner, we will experience a dramatically slowing economy, not just in the U.S. market, but globally as well.

For what it is worth, it seems to me that the regulators must make a dramatic change in the policy of marking to market the valuation of securities that have no market. I would suggest a discounted present value method that includes an adjustment factor for credit quality. Adjusting the credit quality factor can be used in times of market distortions such as is occurring today. Margin calls against loan collateral are causing a cascading withdrawal of money from the financial system. If something is not done about this process, we will see a drop in money supply similar to what occurred in year 2000.

That being said, there exists a window of investing potential. I still recommend buying into this market. Though the potential for a severe deflation is clear, the Fed is, so far, able to hold the money supply to a relatively reasonable contraction in the face of huge margin calls to borrowers. When that is not the case, our Model will pick up the change and recommend reversing our course, I believe.

Almost all of our investors have 30% or more of fixed income in their portfolios. The more fixed income in an investment portfolio, the lower will be the losses as a percent of the market's drop. This last statement applies to stronger, investment grade quality fixed income securities and good quality mortgage backed product.

For those who own leveraged closed end funds as their fixed income component - purchased in order to increase their cash flow income - the market value of these funds has dropped. However, thus far, the dividends paid by these funds have not dropped significantly, and your cash flow has not been impacted greatly. Much work is being done (out of the view of the public) by these fund managers in order to alleviate their liquidity problems due to the shutdown of the auction rate borrowing market. So far, no resolution is apparent, but I expect that one will get done.

In summary, I recommend dollar-cost-averaging new money into the market at this time, and maintaining your existing portfolios at fully invested levels. Note that "fully invested" means a well balanced, diversified and correlated investment portfolio with a fixed income component consistent with your risk tolerance level. Typically, the fixed income component is greater than 30% up to 50% and as high as 70% for some investors.

THUS FAR, THE MODEL CONTINUES TO RECOMMEND FULL INVESTMENT.

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